

II. Overview of County Finances

Butte County's (County) Fiscal Year (FY) 2004-05 Final Budget was adopted by the Board of Supervisors (Board) on August 31, 2004. The FY 2004-05 Final Budget of \$320.9 million increased from the 2003-04 level of \$318.9 million by approximately \$2 million, or 0.62 percent.¹

The County utilized a "target net county cost" budget approach in formulating the FY 2004-05 budget.² Under the "target net county cost" approach, estimated discretionary revenues are made and allocated to departments based on historical distribution. Departments are required to develop a budget to meet the discretionary revenue target. The "target net county cost" approach has the following two benefits:

- Encourages departments to seek alternative funding sources
- Provides flexibility within the department on how available funds can be spent

In addition to applying the "target net county cost" method, the County outlined specific strategies in order to operate within its fiscal limitations. These strategies, which helped to balance the FY 2004-05 Budget include, but are not limited to, the following:³

- Reduce the Vehicle Replacement Fund by \$2,000,000 and transfer those funds to the County General Fund
- Increase Animal Control activity funding through realignment, resulting in \$174,000 in additional discretionary dollars
- Issue Pension Obligation Bonds to pay the County contributions to the Public Employment Retirement System that exceed \$58 million, resulting in a net savings over \$350,000 in the County General Fund
- Implement a retirement incentive plan that provides a net savings of \$175,000 in the County General Fund and provides opportunities for employees currently occupying positions slated to be eliminated, to maintain their employment
- Implement Phase Two of the cost recovery project that will result in an estimated \$1.2 million in discretionary revenue to the County General Fund from charges for services
- Transfer \$1.2 million from the Public Health Trust Fund to the Social Services Trust Fund to augment the social service budget

¹ Butte County 2004-05 Final Budget, Schedule 1 and Butte County 2003-04 Final Budget, Schedule 1

² Butte County Application, p. 46

³ Butte County 2004-05 Final Budget, A-2

Budgeted Expenditures by Fund

In total, the County's FY 2004-05 Final Budget is balanced at approximately \$320.9 million. The General Fund comprises \$154.8 million of the total budget. Various restricted funds, both countywide and less than countywide, comprise the remaining balance:⁴

Budgeted Expenditures FY 2004-05 Final Budget

					Total Financing Requirement		
Countywide:							
	General Fund				\$ 154,811,501	48.24%	
	Welfare				125,702,743	39.17%	
	Child Support Services				9,121,532	2.84%	
	Road Operations				11,869,723	3.70%	
	Debt Services				-	0.00%	
	Capital Projects				276,307	0.09%	
	Equipment Replacement				312,702	0.10%	
	ISF Equipment Replacement				3,173	0.00%	
	State COPS Program				851,811	0.27%	
	Water Services				998,750	0.31%	
	Library				2,243,128	0.70%	
	Fish & Game				24,958	0.01%	
		Sub-total			306,216,328	95.43%	
Less than Countywide							
	Fire Protection				13,919,098	4.34%	
	Local Transportation Fund				486,248	0.15%	
	Housing & Comm. Dev. Fund				273,077	0.08%	
		Sub-total			14,678,423	4.57%	
TOTAL					\$ 320,894,751	100.00%	

The distinction between countywide and less than countywide funds is that the former provides services to all county residents while the latter provides services to the unincorporated area. The General Fund is the primary operating fund of the County. It accounts for all financial resources, except those required to be accounted for in other funds. The Special Revenue Funds account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes. This category of funds includes the following: Welfare Fund, Child Support Services Fund, Road Operations Fund, Debt Service Fund, Capital Projects, Equipment Replacement Fund, State Citizens Option for Public Safety (COPS) Program Fund, Water Services Fund, Library Fund, and Fish and Game Fund. The Special Revenue Fund category also includes the following less than countywide funds: Fire Protection Fund, Local Transportation - Transit Fund, and Housing and Community Development Fund.

⁴ Butte County 2004-05 Final Budget., Schedule 1

Financing Sources

Revenue sources proposed by the County to fund its FY 2004-05 budgetary expenditures are listed below.⁵ As illustrated, state and federal funding along with Property Tax and Charges for Services are the largest sources of funding.

Revenue Sources FY 2004-05 Final Budget

	<u>General Fund</u>		<u>Total Funds</u>	
Property Tax	\$ 24,939,977	16.11%	\$ 24,939,977	7.58%
Other Tax	8,667,673	5.60%	8,667,673	2.64%
Licenses & Permits	4,507,856	2.91%	4,565,856	1.39%
Fines, Forfeit, Penalties	1,879,023	1.21%	1,899,981	0.57%
Use of Money & Property	1,907,700	1.23%	1,986,700	0.60%
Governmental Revenues	-	0.00%	-	0.00%
State Revenues	67,111,145	43.35%	145,806,508	44.33%
Federal Payments	8,087,343	5.22%	70,773,110	21.52%
Other Intergovernmental	3,247,454	2.10%	5,155,486	1.57%
Charges for Services	19,612,997	12.67%	22,461,028	6.83%
Misc. Revenue	3,496,994	2.26%	4,041,580	1.23%
Other Rev. (Trans. to other Funds)	2,589,555	1.67%	19,752,673	6.01%
subtotal	146,047,717	94.33%	310,050,572	94.28%
Fund Balance (As of June 30, 2004)	8,771,151	5.67%	16,505,737	5.02%
Cancellation of Prior Year Reserves/Designations	-	0.00%	2,319,398	0.71%
TOTAL	\$ 154,818,868	100.00%	\$ 328,875,707	100.00%

Budgeted Expenditures by Major Program

The County's programs and adopted FY 2004-05 appropriation amounts are listed below.⁶ As illustrated, Public Assistance is a significant portion of total funding. However, it represents only a small portion of General Fund expenditures.

⁵ Butte County 2004-05 Final Budget, Schedule 5

⁶ Butte County 2004-05 Final Budget, Schedules 7 & 8

Expenditures by Major Program
FY 2004-05 Final Budget

			General Fund		Total Funds	
General Government			\$ 30,862,090	19.94%	\$ 31,276,647	9.81%
Public Protection			59,361,681	38.34%	75,982,201	23.83%
Public Ways & Facilities			-	0.00%	12,355,971	3.86%
Health & Sanitation			57,899,769	37.40%	57,899,769	18.16%
Public Assistance			508,935	0.33%	134,958,009	42.32%
Education			241,046	0.15%	2,484,174	0.78%
Recreation			321,902	0.21%	321,902	0.10%
Contingencies & Reserves			5,616,078	3.63%	5,616,078	1.76%
Provisions for Designations			-	0.00%	(1,984,720)	-0.62%
TOTAL			\$ 154,811,501	100.00%	\$ 318,910,031	100.00%

Mandated Expenditures

The County stresses that it continues to lack flexibility over its general purpose revenue allocations. The County states that it is required or mandated by state law to administer a variety of health care, welfare, and public safety programs. In Butte County's Application for Finding of Significant Financial Distress (Application), the County states that 78 percent of total revenue is restricted. The remaining 22 percent, or \$70.4 million, represents general purpose revenue. Of this \$70.4 million, 35 percent, or \$24.7 million, funds state mandated costs and state established required maintenance of efforts.⁷

The following table illustrates the County's mandated general purpose revenue expenditures:

⁷ Butte County response to staff questions, dated March 30, 2005, Fiscal Question # 12

Mandated Expenditures From General Purpose Revenues
FY 2004-05 Final Budget

Maintenance of Effort			
Public Health	\$724,308	2.94%	
Mental Health	\$424,727	1.72%	
CalWORKS	\$1,264,015	5.12%	
Consolidated Courts	\$748,297	3.03%	
Public Safety Sales Tax (excludes Jail)	\$2,886,591	11.70%	
Child Welfare Services	\$1,690,000	6.85%	
Public Library Funds	\$2,359,719	9.57%	
Sub total	\$10,097,657	40.93%	
State Mandated Programs			
Public Defender	\$1,898,024	7.69%	
General Assistance	\$1,000,000	4.05%	
Grand Jury	\$63,917	0.26%	
County Jail	\$10,657,130	43.20%	
LAFCo	\$164,000	0.66%	
Youth Correctional Placements	\$250,687	1.02%	
Juvenile Court Wards	\$1,820	0.01%	
Foster Care (SED)	\$420,000	1.70%	
Sub total	\$14,455,578	58.59%	
State Mandated County Match			
Welfare Aid Payments	\$0	0.00%	
Court Ordered Payments			
Jail Consent Decree	\$118,096	0.48%	
TOTAL	\$24,671,331	100.00%	

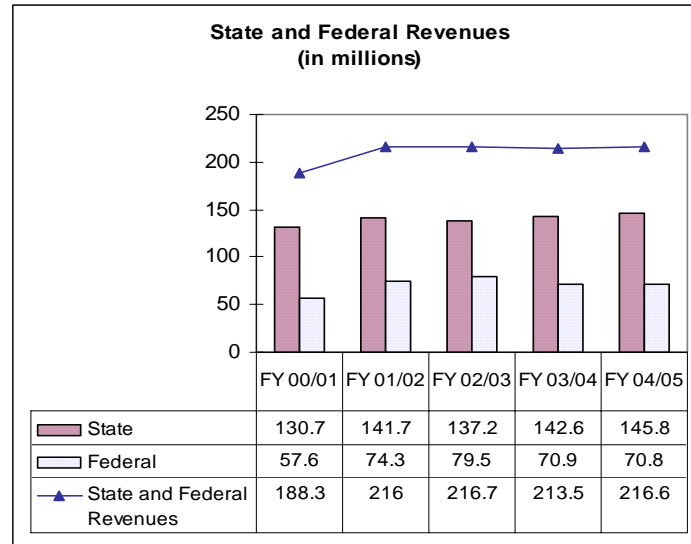
The remaining 65 percent, or \$45.7 million (14 percent of the total budget), of the general purpose revenue is considered discretionary resource and funds basic county services.

Staff notes that the services funded by non-mandated general purpose revenue cannot automatically be considered non-essential county services. Examples illustrating the essential use of general purpose revenue include funding to meet maintenance of effort required for receiving state revenue for public safety and health services and unfunded state mandated programs. Staff further notes that the presence or absence of a state or federal mandate for conducting an activity cannot be the sole indicator of an activity's value, as can be illustrated by libraries which are not state or federally mandated, but may still be a local community priority.

The County's measures to manage its spending for mandated and non-mandated activities are discussed in Sections III and IV of this analysis.

Financial Condition

The County attributes its struggle to provide basic county services to a combination of the following: increased mandated costs in areas like social service programs, increased employee benefits costs, the suspension and deferral of reimbursements of mandated costs, increased contract costs for fire suppression services with the California Department of Forestry (CDF), an increase in the shift of local county property tax revenues to Education Revenue Augmentation Fund (ERAF) and the impact of the “triple flip” provisions. As illustrated below, state and federal revenues have leveled since FY 2000-01.⁸



Further, the total amount of discretionary resources available is expected to decline by \$4 million to \$70.4 million in FY 2004-05 from \$74.4 in 2003-04.⁹

The Legislative Analyst’s Office (LAO) issued a report dated February 22, 2005 titled, “The 2005-06 Budget: Perspective and Issues.”¹⁰ In the report, the LAO addresses state mandate liabilities due to local governments. The state has delayed reimbursements for local governments’ mandate reimbursement claims to cope with its financial difficulties. Consequently, the LAO estimates that the state will owe \$2.8 billion to local governments at the end of FY 2004-05. State obligations include the following:

- About \$2.2 billion for unpaid claims from FY 2004-05 and earlier years
- Over \$500 million for unpaid claims in FY 2004-05
- \$100 million for new mandates identified by the Commission

⁸ Butte County 2004-05 Final Budget, Schedule 5 for 2002-03 through 2004-05

⁹ Butte County Application, p. 62

¹⁰ See Attachment 6 for LAO 2005-06 Perspective and Issues

A portion of these liabilities is owed to the County. In FY 2006-07, the state will begin repaying its prior year mandate liabilities over a five-year period.¹¹ See Section IV. Review of Resource Flexibility for a list of mandates and amounts owed to the County by the state. For the FY 2005-06 budget, and every subsequent year, article XIII B, section 6, subdivision (b) of the California Constitution now requires the Legislature to either appropriate in the annual Budget Act, the full payable amount that has not been previously paid, or suspend the operation of the mandate for the fiscal year.

As presented below, demands outside of the County's growth in programs and services are increasing.¹²

Growth of Programs and Services

<u>Program</u>	<u>FY 02-03</u>	<u>FY 03-04</u>	<u>FY 04-05</u>	<u>Increase from FY 03-04</u>
Social Services Costs exceed Realignment Revenue	2,652,217	4,057,827	2,784,551	(1,273,276)
PERS increase	-	3,459,729	8,761,001	5,301,272
Deferred Approved State Mandates	-	3,806,292	500,000	(3,306,292)
Child Support Penalty	-	63,600	-	(63,600)
CDF Contract Increase	312,642	1,704,394	2,373,326	668,932
TOTAL	2,964,859	13,091,842	14,418,878	1,327,036

Projected demands for these increases amount to additional County expenditures of approximately \$14.4 million for FY 2004-05.

The County's four primary sources of general purpose revenues include the following: property tax, motor vehicle in-lieu fee, sales tax, and Prop 172 sales tax for public safety.

The estimated general purpose revenue sources for FY 2004-05 are as follows:¹³

¹¹ Government Code section 17617, added by Senate Bill 1096, a budget trailer bill (Stats. 2004, ch. 1011, eff. August 5, 2004.).

¹² Butte County Application, p. 6

¹³ Butte County Application, p. 10

Estimated General Purpose Revenue Sources
FY 2004-05 Final Budget

General Purpose Revenue				
Property Tax		\$	24,939,977	40.47%
Motor Vehicle In-Lieu Fee			4,600,000	7.46%
Sales Tax			3,136,445	5.09%
Proposition 172 Sales Tax for Public Safety			11,780,000	19.11%
Other			17,173,428	27.87%
TOTAL			\$61,629,850	100.00%

The property tax retained by the County will increase in FY 2004-05. The passage of Proposition 57, the California Economic Recovery Bond Act, triggered the shift in revenues known as the “triple flip”. Under the old tax rate, 1.25 percent of the statewide sales tax rate of 7.25 percent was allocated to local governments. However, beginning July 1, 2004, the local government portion of the sales tax is decreased by 0.25 percent to pay off the bond. To make up for the loss of sales tax revenue, under the new tax rate, local governments receive an increased share of property taxes. Further, in 1998 the Legislature adopted a schedule of the vehicle license fee (VLF) rate reductions, as a result, the rate fell from 2 percent to 0.65 percent.¹⁴ Under the old tax rule, the state paid the difference to counties. However, VLF back fill is eliminated in FY 2004-05. Therefore, the loss of VLF revenue is exchanged for property tax. However, local agencies will not receive the full amount of the VLF/property tax exchange until FY 2006-07. The state will retain approximately \$700 million in FYs 2004-05 and 2005-06. The County’s portion of the contribution is estimated to be \$1,968,640.¹⁵ See Section IV. Review of Resource Flexibility for discussion on VLF/property tax exchange until FY 2006-07. As a result of these shifts in tax revenues, the County projects the property tax will increase by approximately \$9.2 million, or 58 percent in FY 2004-05 from 2003-04. Both the sales tax and VLF fee revenues are projected to decrease by \$0.7 million, or 18 percent and \$6.3 million, or 57 percent, respectively. The Proposition 172 safety sales tax is also expected to decrease in FY 2004-05 by 1.5 percent, a \$175,974 reduction in revenue from FY 2003-04.¹⁶ See Section IV. Review of Resource Flexibility on four primary sources of general purpose revenues for further discussion.

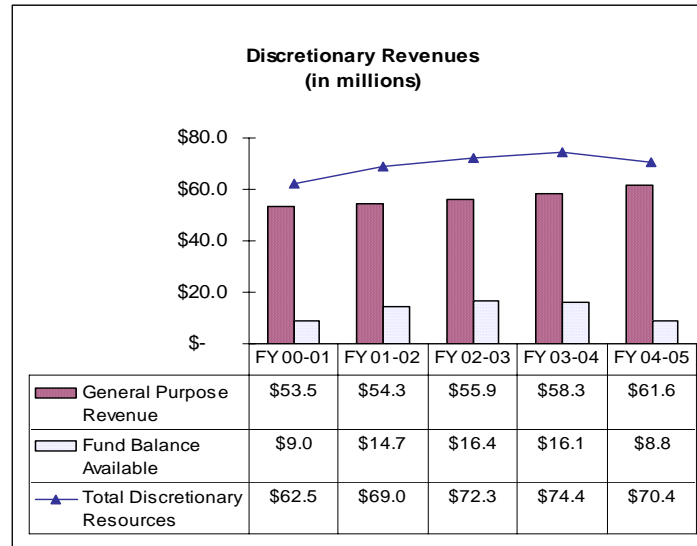
General purpose revenue has gradually increased from \$53.5 million in FY 2000-01, to \$58.3 million in 2003-04, and to \$61.6 million in 2004-05. Despite the fact that the FY 2004-05 general purpose revenues have increased by \$3.3 million from 2003-04, the total amount of discretionary resource available in the 2004-05 Final Budget is \$70.4 million. This represents a \$4 million, or 5.4% decrease in discretionary revenues from FY 2003-04 as presented below:¹⁷

¹⁴ Assembly Bill 2797, Chapter 322, Statute of 1998

¹⁵ Butte County 2004-05 Proposed Budget, Budget Message, p. 9

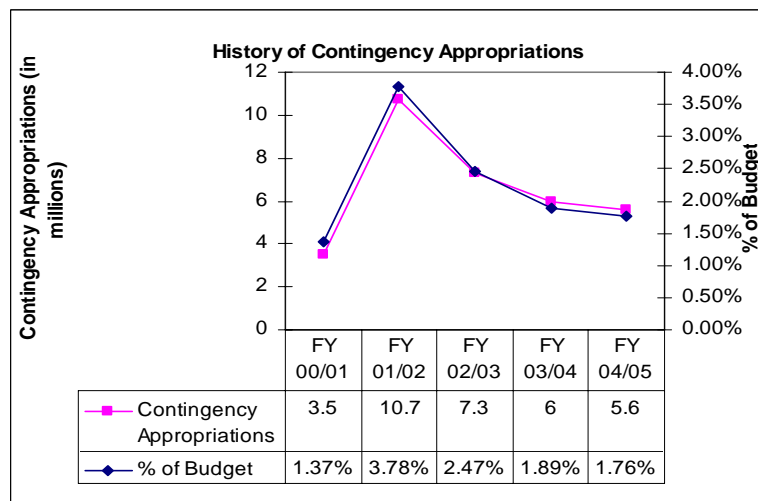
¹⁶ Butte County 2004-05 Final Budget, Schedule 5

¹⁷ Butte County Application, p. 62



One of the reasons for the decline in the fund balance available for FY 2004-05 is the loss of the vehicle license fee “gap” funding in 2003-04. This resulted in a reduction of \$4.3 million to the County.¹⁸ Additionally, the County received less interest income than expected in FY 2003-04.

The County’s contingency appropriation peaked in FY 2001-02 and has continued to decline. It is expected to decrease by \$.4 million from \$6 million in FY 2003-04 to \$5.6 million in 2004-05 as presented below:¹⁹



See Section IV. Review of Reserve Resource Flexibility, for further discussion.

¹⁸ Per the Butte County 2004-05 Proposed Budget, p. 9, the state will schedule to repay the VLF gap loan in 2006-07

¹⁹ Butte County Application, p. 66

General Assistance Savings

The County previously received findings of significant financial distress from the Commission on two instances: On October 29, 1996, the County received a 12-month finding of significant financial distress from the Commission. The original finding was extended for a period of 36 months and expired on December 28, 1999; and on November 30, 1999, the County received the second finding of financial distress that expired December 28, 2002²⁰.

The County states that it once again finds itself in fragile financial straits to maintain current program and service levels. Consequently, on February 10, 2005, the County filed an Application for Finding of Significant Financial Distress in accordance with Senate Bill 1033.²¹ Based on the information provided by the County, staff estimated that a 12-month General Assistance (GA) rate reduction would result in general purpose revenue savings upon the approval of the distressed county designation of approximately \$269,280.²² See Section IV. Review of Resource Flexibility for further discussion.

Recommendation on County Finances

Staff recommends that the Commission find that:

- **The County's FY 2004-05 Final Budget totals \$320.9 million, with a General Fund contingency appropriation of \$5.6 million. While this represents increased financing requirements of approximately \$2 million from prior year, the General Fund contingency is expected to decrease by \$0.4 million.**
- **The County's discretionary expenditure flexibility is constrained both by fund restrictions and by state and federal mandates, leaving \$70.4 million, of the \$320.9 million in Final Budget appropriations, as theoretically available for discretionary use.**
- **The full \$70.4 million cannot be considered truly discretionary since 35 percent, or \$24.7 million, is directed toward state mandated costs and state established required maintenance of efforts.**

²⁰ Butte County Application, p. 1

²¹ Senate Bill 1033, Chapter 72, Statute of 1993

²² Butte County Application, p. 3 and Butte County response to staff questions, dated March 30, 2005, Fiscal question # 10

Cost savings is computed based on the following steps: 1) Compute the difference between the current GA rate and proposed reduced GA rate; 2) Compute the monthly cost savings by multiplying the difference computed in the step 1) by the number of monthly GA recipients; and 3) Compute annual savings by multiplying the monthly savings by 12. The number of monthly General Assistance recipients is estimated as follows: average monthly number of recipients for 2000-01 through 2003-04 is 329 $((313+305+341+355)/4)$. The monthly average for 2004-05 is 330 (up to February). Consequently, 330 appears to be a reasonable estimate for the number of monthly recipients for 2004-05.

Cost savings would be: $\$269,280 = (\$289-\$221)*330*12$.

- **The County's total available discretionary resource for FY 2004-05 is projected to decline by \$4 million from \$74.4 million in FY 2003-04 to \$70.4 million in FY 2004-05.**
- **Demands, such as retirement benefit contributions, CDF contract costs, and reduced reimbursements funded through state mandate claims are increasing.**